No. 94-1010

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In the Supreme Court of the United States

OCTOBER TERM, 1994

NATIONAL UNION FIRE INSURANCE COMPANY,

PETITIONER,

v.

CNA INSURANCE COMPANIES AND
COLUMBIA CASUALTY COMPANY,

RESPONDENTS.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS TO THE FIFTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

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QUESTION PRESENTED

Did the United States Court of Appeals for the Fifth Circuit correctly interpret a specially negotiated insurance contract under Texas law when it affirmed a summary judgment against Petitioner on claims that Respondent insurer failed to settle a claim within policy limits, despite the fact that Respondent had no authority under the insurance contract to settle claims and had received no settlement demand from the claimant within policy limits?

LIST OF PARTIES

In accordance with Rules 14(b) and 29.1, the list of all parties to this proceeding includes:

Petitioner: National Union Fire Insurance Company

American International Group, Inc. is the parent of Petitioner National Union Fire Insurance Company.

Respondents: CNA Insurance Companies *
Columbia Casualty Company, Respondent

Continental Casualty Co. is the parent of Respondent Columbia Casualty Company. CNA Financial Corp. is the parent of Continental Casualty Co. Loews Financial Corp. owns 80% of the stock of CNA Financial Corp. Respondents have no non-wholly owned subsidiaries.

* "CNA Insurance Companies" is not a legal entity and was not a proper defendant below. Rather, "CNA" is a registered service mark and "CNA Insurance Companies" is a fleet name used by a number of insurance companies, including Columbia Casualty. Both Columbia Casualty and CNA will be referred to collectively as "Columbia Casualty" herein.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1 to A-10) is reported at 28 F.3d 29. The opinion of the district court (Pet. App. A-11 to A-29) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 10, 1994, and a petition for rehearing was denied on September 6, 1994 (Pet. App. A-30 to A-31). The petition for a writ of certiorari was filed on December 1, 1994. By letter dated January 12, 1995, the Court extended the time for responding to the petition through February 6, 1995. Respondents do not contest Petitioner's jurisdictional allegations under 28 U.S.C. §1254(1).

STATEMENT OF THE CASE

This is a diversity case decided under Texas law. Petitioner, National Union Fire Insurance Company, an upper layer excess carrier, sued Respondent, Columbia Casualty Co., a lower layer excess carrier, alleging that Columbia Casualty wrongfully failed to settle a claim against their common insured within the limits of the Columbia Casualty policy. The United States Court of Appeals for the Fifth Circuit affirmed the summary judgment granted by the district court in favor of Respondent. The Fifth Circuit held that Columbia Casualty did not breach a duty to settle because, under the specially negotiated terms of the policy, the insured retained the right to control the defense and to settle. The Fifth Circuit held that there was no evidence in the record that Columbia Casualty took over the control of the defense. (Pet. App. A-9).

Ariens Company, the insured, manufactured motorized lawn equipment. In 1976, Ariens chose to self-insure and to control its own litigation because it became dissatisfied with its insurance carrier's pattern of decision-making regarding the defense and settlement of claims against it. Ariens negotiated a "special manuscript" excess insurance policy with Columbia Casualty. The policy provided that Ariens would be self-insured up to $100,000 per occurrence, and $750,000 in the aggregate. Columbia Casualty provided the first layer of excess coverage between the self-insured limit of $100,000 and up to $1 million. Columbia Casualty also provided a second layer of excess coverage, up to $5 million in the aggregate. National Union issued the top layer of coverage to Ariens, providing up to $15 million in coverage above Columbia Casualty's second excess policy.

In 1985, Ariens was sued by the parents of a four-year old boy who lost both hands and part of his arm while operating an Ariens riding mower. The plaintiffs alleged that the mower was defective because it did not have a switch that killed power if the rider left the mower's seat. Ariens hired its own lawyers to defend the suit. Prior to trial the plaintiffs never made a settlement demand, nor engaged in settlement negotiations with Ariens. During the trial the plaintiffs made a $7.5 million settlement offer. Ariens rejected this offer, which exceeded Columbia Casualty's limits by $2.5 million. After trial the jury awarded the plaintiffs $22.5 million, which the district court remitted to $15 million. Ultimately, Ariens settled with the

plaintiffs for $7.5 million. Columbia Casualty paid $4.9 million under its two excess policies and National Union paid $2.5 million under its top-layer excess policy.

After conclusion of the litigation, National Union sued Columbia Casualty in Texas state court, contending that it breached a duty — either direct or indirect — by not settling the case before trial. Columbia Casualty removed the case to the United States District Court for the Eastern District of Texas on grounds of diversity.

The district court entered summary judgment against National Union. Central to the district court's reasoning was that the insurance contract unambiguously shifted control of the defense of the suit to Ariens, including handling settlement discussions. Columbia Casualty retained only the right to "voluntarily become associated with the defense or negotiations against Ariens, [but] in no way obligated itself to associate." (Pet. App. A-19). The district court also found that "there was never any settlement negotiation for Columbia Casualty to associate with," and that the plaintiffs never made a settlement demand before trial. (Pet. App. A-20, 24-25). The district court reached the common-sense conclusion that under Texas law, Columbia Casualty could not be liable for failing to settle the case within policy limits. The court of appeals affirmed.

ARGUMENT AND AUTHORITIES

This case is not worthy of *certiorari*. It involves a contract dispute between private litigants under Texas law. The United States District Court for the Eastern District of Texas and the United States Court of Appeals for the Fifth Circuit both reached the same, correct, result. Petitioner asks the Court to ignore Texas Supreme Court precedent and change established Texas law.

National Union's petition should be denied because:

- This case involves the application of Texas law by a federal district court and court of appeals.
- This case will have little, if any, precedential effect because it involves construction of a contract under Texas law.
- The factual posture of this case prevents the court from reaching the merits of petitioner's alleged errors in applying Texas law.
- The district court and Fifth Circuit correctly interpreted and applied Texas law.

A. This Case Involves Application Of Texas Law By A Federal District Court and Court Of Appeals

The lower courts correctly applied Texas law. Both the United States District Court for the Eastern District of Texas and the United States Court of Appeals for the Fifth Circuit applied Texas law, reached the same result, and employed the same reasoning. Historically, the Court has

been reluctant to review the application of state law by intermediate federal appellate courts, especially when, as in this case, the appellate court applied the law of a state within its circuit. The Court should defer to expertise of these federal courts in Texas that frequently resolve issues of Texas law.

In 1980, when the Court restated what is now Rule 10.1 describing considerations governing review on *certiorari*, the Court specifically omitted predecessor Rule 19(1)(b) that gave *certiorari* relevance to a court of appeals decision resolving "an important state or territorial question in a way in conflict with applicable state or territorial law." In doing so, the Court delegated resolution of questions of state law almost exclusively to the federal courts of appeals. *Haring v. Prosise*, 462 U.S. 306, 314 n.8 (1983) ("[w]e emphasize . . . that, standing alone, a challenge to state-law determinations by the court of appeals will rarely constitute an appropriate subject of this Court's review."). Such deference is particularly appropriate where, as in this case, the district court and the court of appeals agree in their views of state law. *See Bishop v. Wood*, 426 U.S. 341, 356 (1976).

Similarly, where the Court has granted *certiorari* for other reasons, it frequently has deferred to the views of the court of appeals as an expert tribunal on the laws of the states within its circuit. *Brockett v. Spokane Arcades, Inc.*, 472 U.S. 491, 499-500 (1985); *Butner v. United States*, 440 U.S. 48, 57-58 (1979). The Court should defer to the

opinions of both Texas federal courts that considered the Texas law issues in this case.

B. This Case Will Have Little, If Any, Precedential Value Because It Involves Construction Of A Specially Negotiated Contract Under Texas Law

The district court resolved this case based on its interpretation of unambiguous language in a special manuscript insurance policy that Ariens and Columbia Casualty negotiated. This language amended the standard form policy and allowed the insured to retain control over its own defense and to settle claims. In its place, the parties substituted language allowing Columbia Casualty to voluntarily associate in the defense or settlement negotiations, but leaving control of the defense and settlement with Ariens. The insurers could not settle claims without the insured's consent.

National Union seeks damages, arguing that Columbia Casualty should have negotiated and consummated a settlement with the claimant beneath the limit of National Union's excess coverage. The Fifth Circuit affirmed the district court's holding that the specially negotiated terms in Ariens' policy did not give Columbia Casualty the right to settle claims. Columbia Casualty could not have a legal duty to do something that it had no legal right to do.

Any opinion the Court could issue would have extremely limited precedential value. An opinion

necessarily would affect only other self-insured entities that retained control over their own litigation defense and settlement, and that have at least two levels of excess coverage underwritten by different companies. Any precedential value of this case would further be limited to such insurance arrangements within Texas. There are certainly better uses for the Court's limited resources than opining on narrow, contract-specific questions such as those presented in this case.

C. The Factual Posture of This Case Prevents The Court From Reaching The Points Argued By Petitioner

National Union argues that summary judgment was improper because the record raised fact issues for the jury. National Union is wrong. Two recent Texas Supreme Court decisions require that the judgment of the lower courts be affirmed without even reaching the points argued by National Union in its Petition.

One important fact remains undisputed: ***the claimant in the underlying case never made a settlement demand within the limits of Columbia Casualty's coverage.*** This fact disposes of all the issues in this case. The Texas Supreme Court has held that absent a demand by the claimant to settle within policy limits, the insurer has no duty to settle a claim against its insured. *Texas Farmers Ins. Co. v. Soriano*, 881 S.W.2d 312, 317-18 (Tex. 1994). Even if the policy had given Columbia Casualty the right to control defense of the litigation and to settle claims against

Ariens, or if Columbia Casualty had voluntarily taken over defense of the case, it would have no bearing on the outcome of this case because the claimant never made a settlement demand within the limits of Columbia Casualty's coverage.

Texas first recognized the duty of an insurer to settle within policy limits under certain circumstances in *G.A. Stowers Furniture Co. v. American Indem. Co.*, 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved). The *Stowers* doctrine has remained an entrenched part of Texas law for over sixty years. For most of this time, the courts assumed that an essential element to a *Stowers* claim was a demand from the claimant within the limits of insurance coverage. In *Soriano*, the Texas Supreme Court confirmed that a demand within the policy limits is a necessary prerequisite to a *Stowers* claim. *Soriano*, 881 S.W.2d at 314-15. It is undisputed that the only settlement demand in this case was for $2.5 million ***in excess*** of Columbia Casualty's coverage.

National Union repeatedly argues that Columbia Casualty should have negotiated a "better deal" with the claimant to reduce the settlement to an amount within the limits of the Columbia Casualty coverage. This argument ignores Texas Supreme Court precedent and the language of the insurance policy. The Texas Supreme Court in *Soriano* rejected this specific argument: "regardless of how reasonable the demand, unless there is a demand within the policy limits, no *Stowers* claim will exist." *Soriano*, 881

S.W.2d at 314-15. In addition, the unambiguous language of the insurance policy gave Ariens control over settlement.

National Union has no claim against Columbia Casualty unless Columbia Casualty had a *Stowers* duty to settle the claim against Ariens within policy limits. The Texas Supreme Court has refused to recognize a direct duty running from a lower-level insurance carrier to an upper-level insurance carrier. *American Centennial Ins. Co. v. Canal Ins. Co.*, 843 S.W.2d 480, 483 (Tex. 1992). National Union can only assert a claim against Columbia Casualty through equitable subrogation to a *Stowers* claim which the insured would have had but for the excess coverage. *Id.* Ariens never had a *Stowers* claim against Columbia Casualty because the claimant never made a settlement demand within the limits of Columbia Casualty's coverage. Thus, National Union could not have acquired a claim against Columbia Casualty by subrogation. The lower courts reached the correct result based on the undisputed facts.

D. The District Court And The Fifth Circuit Correctly Interpreted And Applied Texas Law

The Fifth Circuit followed controlling Texas Supreme Court precedent in disposing of National Union's claims. The Fifth Circuit followed *American Centennial* in holding that Columbia Casualty owed no direct duty to National Union. The Fifth Circuit followed *Soriano* and *Stowers* in rejecting National Union's indirect duty claim. To hold in

favor of National Union, the Court would have to overrule the Texas Supreme Court on a matter of Texas law.[1]

In an attempt to circumvent the clearly established Texas case law, National Union argues that Columbia Casualty "took over" defense of the case by voluntarily participating in settlement discussions. The Fifth Circuit correctly rejected this argument:

> First, the terms of the policy unambiguously reserve control of the defense to Ariens, and not Columbia. Thus, as a matter of law, Columbia Casualty could not have controlled the defense of the claim. Second, the summary judgment evidence which National Union cites in its brief demonstrates at most that Columbia's adjuster participated in settlement negotiations with the *Hines* plaintiffs. We have held as a matter of law that where the insured has retained independent counsel, an insurer's participation in settlement negotiations did not itself constitute an assumption of the insured's defense. *Arkwright-Boston Mfrs. Mut. Ins. Co. v. Aries Marine Corp.*, 932 F.2d 442 (5th Cir. 1991).

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[1]In addition to its direct and indirect duty claims, National Union raised Texas statutory claims under the Texas Deceptive Trade Practices Act and the Texas Insurance Code. However, the statutory claims were predicated on there being a duty running from Columbia Casualty to National Union, and the Fifth Circuit found these claims necessarily disposed of by the district court's ruling that no duty existed. (Pet. App. A-10).

Pet. App. A-9.

The insurance policy specifically provided that Ariens retained the right to control its own defense, and to approve or reject any settlement offers. Ariens hired its own attorneys to defend the case. Columbia Casualty never refused to consent to a settlement offer that Ariens wanted to take. Under Texas law, Ariens could state no claim against Columbia Casualty for failure to settle within the underlying policy limits. Because Ariens had no claim against Columbia Casualty, National Union could not possibly acquire one through equitable subrogation.

CONCLUSION

This case does not merit *certiorari*. Petitioner urges an unnecessary investigation into settled Texas law that was correctly applied by both lower courts. Recent Texas Supreme Court decisions in *American Centennial* (refusing to recognize the existence of a direct duty owed by primary carriers to excess carriers) and in *Soriano* (holding that a *Stowers* claim requires proof of an actual settlement demand within policy limits) underscore the correctness of the results reached by the lower courts. The Court should deny the Petition for Writ of Certiorari.

Respectfully submitted,

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